NOTES

WASHINGTON NOTES

REMOVAL OF GOLD EMBARGO

The Federal Reserve Board on June 9 announced the removal of the gold embargo and the rescinding of all restrictions upon dealings in foreign exchange. This terminates an experiment unique in American financial history which has now lasted about twenty-one months. During that time there has been absolute prohibition of any exportation of gold or silver without special permission of the Federal Reserve Board, while during the last eighteen months of the period there has been a very close control of dealings in foreign exchange, practically nothing being done without definite permission from the Board or the Treasury Department or both. This system was installed in rather close imitation of that established by Great Britain, its purpose being that of "conserving" the metallic supply and hence of keeping it available for use in bank reserves. Coupled with this effort was the attempt to induce the public to cease using gold or gold certificates in ordinary circulation and to turn them into the banks in order that they might be employed in building up the reserves of those institutions. The latter effort has been largely successful but the control of gold and exchange has been, according to the best opinion, of more than doubtful value. It is a well-known fact that the installation of the system was opposed by some of the government's financial advisers, it being their view that the United States was strong enough to hold its own and retain its gold, a position which has been repeatedly demonstrated during the war. On the other hand, the experience in exchange relations with foreign countries has been most disappointing and regrettable, almost warranting without reference to any other consideration the idea of retaining an open gold market. It is admitted on all sides that could such a market have been maintained in the United States, the gain in prestige and advantage to the country would have been so great as practically to have warranted slight losses of gold, had such occurred, even from the standpoint of the gold conservationists. The theory of the whole proceeding, however, has been fundamentally wrong and this is now generally admitted throughout the world. Bank

inflation is only masked but not prevented or checked by the maintenance of a quantity of gold in the reserves, and the evil of the inflation is equally as serious when a considerable amount of gold (not paid out in redemption of notes or certificates) is kept on deposit. Only a psychological effect is exerted by the presence of the gold and, as experience has abundantly shown, many substitutes for this kind of influence may readily be developed, as they have been in other directions, during the war. The gold embargo and the control of foreign exchange must be essentially regarded as having been little more than an imitation of British policy, not called for in the United States; and, even if defensible there, not so defensible here. The removal of the embargo leaves the United States in a position of advantage as the one really free gold market in the world today. The action of the United States has been taken with the close knowledge and assent of the other Allied countries, and it is to be expected that they may before long follow our example if they do not do so almost immediately. So soon as the restrictions are eliminated, a redistribution of gold is to be looked for, and with regret be it admitted, a movement of the metal toward the United States may very probably be expected. This, if it shall occur, will still further add to the inflationary dangers now recognized.

THE UPWARD MOVEMENT IN STOCKS

One of the notable events of the months of May and June has been the strong upward movement in stocks. This movement has carried both the volume of transactions and level of values to the highest point in three years. On some days transactions have exceeded 2,000,000 shares, while on others they have averaged from 1,500,000 to 1,800,000 for days at a time. With the exception of the railroad stocks, which are regarded as having been stabilized owing to government control, the general movement of all stocks has been strongly upward, while in the oil, motor, and metals groups there has been excited speculation of the most violent order. This speculation resulted early in June in a call money rate of 11 per cent. While an active speculative movement in the past has usually followed the conclusion of war, there are several features of the present situation that are of more than ordinary interest. One of these is the fact that, owing to an unwillingness to pay the excessively high rates of federal taxation, men who bought stocks some time ago at low figures now hesitate to sell them because they know that the bulk of their profits will pass into the hands of the federal government. The effect of this feeling has been to keep the

supply of stocks low, so that many short lines were established before it was realized how the new conditions of taxation and other features would affect the conduct of operators. It is generally agreed that the level of prices established during May and June is not warranted by anything either in the earnings and dividend situation, or (despite the prosperous outlook for the future) in the business prospect of the country. The advance is partly psychological and partly the consequence of peculiar conditions just described with relation to taxation. It would naturally be expected under these conditions that the Federal Reserve Board would take steps to correct the evils complained of, but the present problems of government financing practically preclude such action, inasmuch as an advance in rates of discount designed to shorten the supply of money so as to advance call rates and keep them high (thereby cutting off speculative dealings in consequence of the heightened cost and lessened margin of profit), could not be undertaken because of its reflex effect upon public credit. This indeed has been admitted by the Federal Reserve Board in the Federal Reserve Bulletin for June and constitutes a situation which practically prevents the exerting of real control of stock operations. Probably nothing of an important nature can be done through the ordinary banking channels until such time as further government financing is out of the way, or at least until the dependence upon a low rate of interest is lessened or abandoned. Meantime the effect of the excited speculation is bad in many ways. It tends to render New York an undesirable place for the financing of foreign trade—a field in which it has been hoped that we might become eminent, while on the other hand it opens the possibility of a banking disturbance even more serious than that which exists today. Altogether the recurrence of this speculation is regarded by some as almost warranting an attempt to put once more into effect the restrictions imposed by the Money Pool Committee. As yet nothing definite has been done looking in this direction, although the idea has evidently been contemplated with favor by not a few persons.

THE EXCHANGE SITUATION

Out of the very heavy balance of trade in merchandise between the United States and other countries, there has grown a peculiar situation which now represents perhaps the foremost financial problem connected with the future of American industry and business. This is the method of keeping up and paying for our export operations. The international balance of trade has been running in favor of the United States for the past three years at the rate of about $3,000,000,000 per

annum and now amounts to between $400,000,000 and $500,000,000 per month, or at a moderate estimate, perhaps $5,000,000,000 per annum, should the existing level of exports be maintained. As a matter of fact, careful bankers and financiers estimate that credits of approximately $4,000,000,000 will be required if the present volume of business is to be financed and continued up to December 31. Meantime the government which has been standing behind our trade with foreign countries to the extent of between $9,000,000,000 and $10,000,000,000 since the United States became a belligerent is practically on the point of withdrawing from this kind of support for the future although there still remain some small allowances included in the congressional appropriations which may be applied to the purpose if desired. This apparently means that private methods of financing the business must be evolved; and accordingly banking conferences have been in progress both in Washington and New York during the past month with a view to obtaining a co-operative agreement among bankers designed to support the export trade upon some reasonable level, even if not at its present high figure. The question at issue is apparently how far the United States is warranted in going with the financing of this trade, even assuming that the needed funds can be obtained from its citizens. What is proposed in effect is that this country shall part with very great quantities of goods, turning such goods over to European consumers but getting comparatively little in exchange. The effect of such an operation conducted upon the great scale now proposed is obviously and necessarily that of raising prices in the United States by two methods—that of rendering goods scarce, while credit or money or securities received in payment for the goods are relatively abundant. From the broad social standpoint this situation raises the question whether we can very well afford to aggravate the present high cost of living, or to see prices rise still further above their accustomed and normal level. On the other hand, the question how far European countries can wisely use such advances as it is proposed to make them is fairly to be raised. Considerable quantities of goods and capital can undoubtedly be wisely used in restoring the industrial capacity of Europe, but it would be easy to overdo the extension of credit, especially at a time when European business and manufacturing processes are in confusion and when the disturbance of markets and international trade is such as to cause great uncertainty regarding the future course to be taken by business, as well as the conditions under which competition may be maintained. Some definite arrangement to finance the export trade will be necessary in the near future, since the heavy decline

of continental exchanges such as lire and francs, and the unsteadiness of sterling, make it evident that we cannot expect to see business firms or banks continue to become large owners of foreign currency or bills of exchange due to the apparently continuous depreciation to which they are all subject.

COMPARATIVE PRICE TABLES

A careful study of prices in the United States, England, France, Italy, and Sweden has been prepared for the Department of Commerce and the War Industries Board by W. C. Mitchell, M. L. Goldsmith, and F. K. Middaugh. These figures are drawn from international data representing the best available prices taking the average actual prices during the twelve months preceding the European War as a base figure. The chief conclusions from the comparisons of the English and American price movements are stated as follows:

1. The war-time rise began about a year earlier in England than in the United States.

2. The earlier advance in England opened a wide margin between the English and American price levels, which was fairly constant in 1915 and 1916.

3. The margin was cut down by the sudden upward spurt of prices in the United States when this country entered the war.

4. But the margin became wider again in the latter half of 1917, when English prices continued to rise, while the American Government succeeded in keeping the price level nearly constant.

5. The margin (between prices in England and in the United States during the war period) is much wider than that which prevailed before the war. . . . .

6. The maximum rise of prices exceeded that in the United States by 30 to 40 points, or, say, 15 to 20 per cent of the American index numbers.

This comparative study has suggested to some the desirability of the development of an international price index designed for the purpose of obtaining a basis for the study of prices on a genuinely comparative footing. In order to get such an international index it would be necessary to standardize the lists of commodities and methods of computing index numbers in the several countries in order to assure practically uniform comparative methods. This would necessitate co-operation between the statistical offices of the several countries. It is believed that something of the sort may be developed as an outgrowth of the present study whose results have just been outlined.